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Cases, Regulations and Statutes

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does not include a unit in a hotel, motel, inn or other establishment more than one-half of the units in which are used on a transient basis."[15] In light of those two definitions, it would seem doubtful that an owner-occupied farm or ranch residence would be considered to be "residential rental property."[16]

However, the statute goes on to state that if any portion of a building or structure is occupied by the taxpayer, the gross rental income from the property includes the rental value of the portion so occupied.[17] That provision coupled with the definitions of "residential rental property"[18] and "dwelling units"[19] would suggest that an owner-occupied farm or ranch residence would seem to be 27.5-year property and a business use (assuming the eligible business use does not exceed 20 percent of the total residence)[20] would be depreciable over 27.5 years, at a straight line rate with a mid-month convention.[21]

An important issue is whether a tenant-occupied farm or ranch residence would be similarly classified where the tenant does not pay rental for the right of occupancy. Since the residence is not owner-occupied, the provision imputing the rental value of the portion so occupied as gross rental income from the property[22] would not apply and the definition of "residential rental property" would seem not to apply because 80 percent or more of the gross rental income from the building or structure would not be gross rental income from the building or structure.[23] It is noted that the Internal Revenue Service has ruled that occupancy of a dwelling by a farm tenant does not produce income for the tenant.[24]

Therefore, if a farm or ranch residence occupied by a non-rent paying tenant is not "residential rental property," as would appear to be the case, the property must either be "nonresidential real property,"[25] a farm building[26] or seven-year property (because it is not classified elsewhere).[27] It would seem that status as a farm building (depreciable over 20-years) is the most likely.

In conclusion

Additional guidance from the Internal Revenue Service would be helpful in resolving the question of the proper classification of the farm or ranch residence under various factual circumstances.

FOOTNOTES

1 Pub. L. No. 99-514, § 201, 100 Stat. 2121 (1986).

2 I.R.C. § 168.

3 See generally 4 Harl, *Agricultural Law* § 29.05[2] (2000); Harl, *Agricultural Law Manual* § 4.03[4] (2000).

4 See Rev. Proc. 87-56, 1987-2 C.B. 674 (list of ADR class lives); Rev. Proc. 88-22, 1988-1 C.B. 785 (guidelines for horses).

5 I.R.C. § 168(e)(2)(B), 168(e)(3)(F).

6 *Id*.

7 1987-2 C.B. 674.

8 Hart v. Comm'r, T.C. Memo. 1999-236 (tobacco barn was 20-year property; not eligible for expense method depreciation and not single purpose agricultural or horticultural structure).

9 I.R.C. § 168(d)(1).

10 Treas. Reg. § 1.48-1(e)(1), (2).

11 *Id*.

12 I.R.C. §§ 168(e)(2)(A), 168(c)(1).

13 *Id*. See I.R.C. § 168(b)(3)(B).

14 I.R.C. § 168(e)(2)(A)(i). See Ltr. Rul. 9825024, March 20, 1998 (nursing home business owned by S corporation was residential rental property).

15 I.R.C. § 168(e)(2)(A)(i)(I).

16 See I.R.C. §§ 168(e)(2)(A), 168(c)(1).

17 I.R.C. § 168(e)(2)(A)(ii)(II).

18 I.R.C. § 168(e)(2)(A)(i).

19 I.R.C. § 168(e)(2)(A)(i)(I).

20 See I.R.C. § 168(e)(2)(A)(i).

21 I.R.C. §§ 168(e)(2)(A), 168(c)(1), 168(d)(2).

22 I.R.C. § 168(e)(2)(A)(ii)(II).

23 I.R.C. § 168(e)(2)(A)(i).

24 Rev. Rul. 70-72, 1970-1 C.B. 15.

25 See I.R.C. §§ 168(e)(2)(B), 168(c)(1).

26 I.R.C. §§ 168(e)(2)(B), 168(e)(3)(F).

27 I.R.C. § 168(e)(3)(C)(ii).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

ADVERSE POSSESSION

FENCE. The disputed land was located on an island created by two forks of a river. When the parties' predecessors in interest owned the properties, the island was swamp land. The plaintiff's predecessor in interest constructed a fence on the bank of the southern fork of the river to prevent cattle from reaching the swamp land. When the plaintiff and defendant purchased their neighboring properties, the island had become dry land. The island was included in the plaintiff's title description but the plaintiff's predecessor did not use the land because it was too wet. The defendant was told that the fence was the true boundary between the properties but the plaintiff believed that the fence existed only because of its historical use. The defendant argued that the open possession and use of the disputed land for many years established title by adverse possession. The plaintiff argued that the fence was merely a fence of convenience and could not be the basis of title by adverse possession. The trial court had granted the defendant summary judgment on the issue but the appellate court reversed, holding that the plaintiff had provided enough evidence of the existence of the fence of convenience to require a trial on the issue. **Hovendick v. Ruby, 10 P.3d 1119 (Wyo. 2000)**.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

EXEMPTIONS

PENSION PLAN. The debtor owned an interest in a simplified employee pension plan (SEP) provided by the debtor's employer. The debtor claimed the interest as exempt under Ohio Rev. Code § 2329.66(A)(10)(c) as an individual pension plan. The court held that the Ohio exemption was intended to apply only to individual retirement plans, such as IRAs, and not to pension plans provided by employers or that exceeded the restrictions on individual plans; therefore, the SEP was not eligible for the Ohio exemption. The court noted that another section, Ohio Rev. Code § 2329.66(A)(10)(b), provided for other pension plans but limited the exemption amount to that necessary for the support of the debtor. Because the debtor did not claim any right to that exemption, no holding was made under that exemption. ***In re* Schreiner, 255 B.R. 545 (Bankr. S.D. Ohio 2000)**.

FEDERAL TAX-*ALM* § 13.03[7].*

CLAIM. The debtor filed for Chapter 7 on May 9, 1997 and did not elect to end the tax year on the day before the filing. The debtor timely filed and paid the 1997 taxes but filed a claim in the bankruptcy case for the 1997 taxes. The court held that the 1997 taxes could not be included as a claim because the debtor paid the taxes and the estate was not liable for the taxes because the debtor did not make the election to end the tax year under I.R.C. § 1398(d). ***In re* McCready, 255 B.R. 834 (Bankr. M.D. Tenn. 1999)**.

DISCHARGE. The debtors filed for Chapter 7 in April 1996 and received a discharge of all dischargeable debts in November 1996. In March 1997, the IRS assessed the debtors for 1993 taxes, filed notices of tax liens and sought levy against the debtors' social security payments. The debtors argued that the IRS actions violated the discharge injunction. The court held that the 1993 taxes were not dischargeable in the Chapter 7 case because the tax return was filed less than three years before the filing of the Chapter 7 petition and the taxes were still assessable during the case because the automatic stay tolled the assessment period. ***In re* Khoe, 255 B.R. 581 (E.D. Cal. 2000)**.

SETOFF. The debtor filed for Chapter 7 on May 19, 1998 and the debtor owed taxes from 1993. The case was considered a no asset case so no tax claim was filed by the IRS. The debtor filed and paid 1997 taxes in August 1998, claiming a refund. The debtor was granted a discharge, including the 1993 taxes, in September 1998. The IRS accepted the 1997 tax return but applied the refund to the 1993 taxes. The debtor sought to reopen the Chapter 7 case and listed the tax refund as exempt property. The debtor argued that the tax refund, as exempt property, was not subject to the IRS's right of setoff. The issue was whether Section 522, excluding exempt property from liability for pre-petition debts, or Section 553, allowing setoff of pre-petition debts, controlled where a setoff involved exempt property. The court acknowledged a split of decisions on this issue and held that Section 553 had precedence over Section 522, although the court did not explain the reason for this decision. Therefore, the IRS setoff of the refund against the discharged pre-petition taxes was allowed. The basic reasoning is that, because Section 553 lists several exceptions to the setoff rule and does not include Section 522, the Congress did not intend Section 522 to be an exception to the right of setoff. **United States v. Luongo, 255 B.R. 424 (N.D. Tex. 2000)**.

CONTRACTS

BREACH. The plaintiff was a potato processor and purchased potatoes from the defendant over several contracts. The first three contracts were fully delivered by the defendant but the plaintiff failed to make timely payment on any of the contracts and failed to fully pay for the third contract at the time delivery began under the fourth contract. The defendant started to make deliveries under the fourth contract but stopped when the plaintiff refused to make the delinquent payments on the third contract and to make timely payments on the potatoes delivered so far under the fourth contract. At this time, there was still sufficient time remaining under the contract for the defendant to timely deliver the remaining potatoes if the plaintiff had made timely payment for the potatoes already delivered. The plaintiff purchased potatoes from third parties to cover the remaining potatoes on the fourth contract and sued the defendant for breach of contract. The plaintiff argued that the defendant waived the timely payment requirement by accepting late payments on the first two contracts and continuing to deliver potatoes when past shipments were still not paid for. The court held that no waiver occurred in that the plaintiff provided no evidence of detrimental reliance on the waiver. The court also held that, even if a waiver occurred, the amount of delinquent payments had become so large that it justified stopping deliveries until more payments were made. The plaintiff also argued that it was justified in repudiating the contract and seeking cover once the defendant refused to make further deliveries. The court held that the plaintiff was not justified in repudiating the contract because the plaintiff failed to seek assurance of delivery before repudiation. The court also held that, under Idaho Code § 28-2-609(1), the plaintiff could not justifiably repudiate the contract while delinquent in payment. **Magic Valley Foods v. Sun Valley Potatoes, 10 P.3d 734 (Idaho 2000)**.

COMMERCIAL REASONABLENESS OF RESALE OF GOODS. The defendant had agreed to purchase popcorn from the plaintiff when the popcorn was still growing. The popcorn became contaminated with corn smut on the surface of the stored corn. The parties discussed the situation for several months after which the defendant rejected the popcorn. The plaintiff then attempted to resell the popcorn by sending samples of the popcorn to various buyers. The samples were taken from the worst part of the stored crop. The plaintiff received some offers at half of the original contract price and gave the defendant an option to purchase the popcorn at the highest bid price. The defendant refused and the plaintiff sold the popcorn to another buyer. The plaintiff then sued for the difference between the contract price and the actual price at which the popcorn was sold. The plaintiff argued that the defendant failed to timely reject the popcorn and the defendant countered that the plaintiff did not resell the popcorn in a commercially reasonable manner. The court held that the plaintiff followed standard commercial practice in taking bids and in sending samples of popcorn in the worst condition. The evidence demonstrated that popcorn buyers generally want to see the poorest quality sample in making a bid. The court upheld the jury instruction for timely rejection, holding that the determination of reasonableness of the time and manner of rejection is a fact issue for the jury. **Smith v. Paoli Popcorn Co., 618 N.W.2d 452 (Neb. 2000). See also 587 N.W.2d 660 (Neb. 1999)**.

THIRD PARTY BENFICIARY. The plaintiff ordered two grain dryer systems from a third party which ordered the dryers from the defendant manufacturer. The plaintiff alleged that the dryers were defective and sued the seller and manufacturer. The plaintiff settled with the seller and sought damages in this case from the manufacturer. The plaintiff argued that it was a third party beneficiary of the contract between the seller and the manufacturer based upon two elements: (1) the seller specifically entered into the contract in order to provide the dryers for the plaintiff and (2) the manufacturer required the plaintiff to pay for the dryers by a check made out jointly to the seller and manufacturer. The court held that, under Oklahoma law, these facts were insufficient to impose third party beneficiary rights on the plaintiff as to the contract between the seller and the manufacturer. **Midwest Grain Products v. Productization, Inc., 228 F.3d 784 (7th Cir. 2000)**.

FEDERAL AGRICULTURAL PROGRAMS

ANIMAL WELFARE ACT. The defendant was charged with violation of 7 U.S.C. § 2156 for serving as a referee at a dog fight. The defendant argued that Section 2156 did not apply because the dogs were not transported in interstate commerce, (2) Congress did not have the authority under the Commerce Clause to make the defendant's conduct criminal, and (3) the statute violates the Tenth Amendment to the U.S. Constitution in that it regulates an area reserved to the states. The court upheld the enforcement of Section 2156 because (1) many aspects of the dog fight event involved transportation of people and animals over state lines, (2) Congress may impose criminal sanctions in enforcement of Commerce Clause rules, and (3) the Commerce Clause provides authority of the federal government to regulate activities involving interstate commerce, whether or not also regulated by the state. **United States v. Thompson, 118 F. Supp.2d 723 (W.D. Tex. 1998)**.

CROP INSURANCE. The plaintiff obtained a multi-peril crop insurance policy from the defendant which was reinsured by the FCIC. The plaintiff filed a claim for a crop loss but the defendant denied the claim. The plaintiff brought an action in a state court and the defendant removed the case to the federal court. The plaintiff sought remand back to the state court for lack of a federal question or other federal jurisdictional requirement. The defendant argued that the Federal Crop Insurance Act (FCIA) preempted all state court actions. The court examined the FCIA and found that the act provided for exclusive jurisdiction in the federal courts only for actions brought against the FCIC or USDA under the FCIA, even for actions involving denial of claims by reinsurers. Therefore, the court held that the FCIA did not completely preempt state court actions against reinsurers under the FCIA. The court examined the legislative history of the FCIA and noted that the original bill of the 1994 amendments had included exclusive jurisdiction for actions against reinsurers but that provision was omitted from the final statute. The court noted that the District Court for the Southern District of Texas held to the contrary in *Brown v. Crop Hail Management, Inc., 813 F. Supp. 519 (S.D. Tex. 1993)* although the District Court for the Eastern District of Texas held no preemption in *Bullard v. Southwest Crop Ins. Agency, Inc., 984 F. Supp 531 (E. D. Tex. 1997)*. The court also held that jurisdiction could not be based on a federal question solely from the need to interpret federal regulations and statutes in the case. **Halfmann v. USAG Ins. Services, Inc., 118 F. Supp.2d 714 (N.D. Tex. 2000)**.

LIVESTOCK. The AMS has postponed the effective date, from January 30, 2001 to April 2, 2001, of final regulations which establish a mandatory program of reporting information regarding the marketing of cattle, swine, lambs, and products of such livestock under the Livestock Mandatory Reporting Act of 1999, Pub. L. 106-78; 113 Stat. 1188 (1999), 7 U.S.C. 1635-1636h. See 65 Fed. Reg. 75463 (Dec. 1, 2000), adding 7 C.F.R. Part 57. **66 Fed. Reg. 8151 (Jan. 30, 2001)**.

FEDERAL ESTATE AND GIFT TAX

APPEALS. The administrator of a decedent's estate attempted to file a petition with the Tax Court involving a notice of estate tax deficiency. The petition was sent by private delivery service on the 87th day after the deficiency notice was received, three days before the 90 limitation period expired. The petition was sent on a Friday by overnight delivery but was erroneously marked "hold Saturday." The delivery service held the petition at one of its offices without informing the Tax Court that the package was being held for pickup. The package was held for 12 days and returned to the administrator. The administrator immediately placed the petition in a new envelope and resent the petition to the Tax Court with an explanation for the delay. The Tax Court held that the second mailing would not invalidate the first mailing if the first mailing was properly sent and the first mailing was not improperly addressed because the administrator incorrectly marked the package as "hold Saturday." The Tax Court held that the administrator had submitted the package with sufficient postage, a correct address and sufficient time to be delivered on time to the Tax Court and that the delays were not caused by the administrator's failure to properly send the package; therefore, the petition was held to have been timely filed. **Estate of Cranor v. Comm'r, T.C. Memo. 2001-27**.

MARITAL DEDUCTION. The decedent and surviving spouse owned a house as tenants by the entirety. The property had an outstanding mortgage on the decedent's date of death and the decedent and surviving spouse were jointly and severally liable for the loan. The house passed to the surviving spouse. Under state law, upon the death of the decedent the decedent's estate became jointly and severally liable for the loan with the spouse. Therefore, the IRS ruled that (1) one-half of the fair market value of the house was included in the decedent's estate, (2) the estate could deduct one-half of the loan balance, and (3) the marital deduction equaled the value of the house included in the estate less one-half of the outstanding balance on the loan. **Ltr. Rul 200104008, Oct. 17, 2000**.

POWER OF APPOINTMENT. The decedent and predeceased spouse had established an inter vivos trust, under which at the death of the predeceased spouse, the decedent became the sole trustee and income beneficiary. The trust provided that the decedent as trustee had the power to distribute trust corpus for the decedent's "happiness, health, support and maintenance." The IRS argued that the term "happiness" created a general power of appointment in the decedent; therefore, the trust corpus was included in the decedent's estate. The estate argued that an ascertainable standard existed under Kansas law which governed the decedent's distribution of corpus. Both sides based their arguments on *United States v. Powell, 307 F.2d 821 (1962)* which interpreted the term "happiness" under Kansas law. The estate argued that happiness was a sufficient ascertainable standard unless the trust contained language which expanded the meaning of the term. The IRS argued that the *Powell* court held that the term "happiness" was insufficient unless the trust provided language which limited the meaning of "happiness" to produce an ascertainable standard. The court agreed with the IRS and held that, because the trust here did not have any limiting language, the decedent had a general power of appointment over the trust corpus sufficient to include the trust corpus in the decedent's estate. The estate argued that the trust had limiting language in that (1) happiness was tied to health, support and maintenance, (2) the trust provided for remainder beneficiaries, and (3) the trust had a spendthrift clause. The court held that these provisions did not place any limitation on the "happiness" provision sufficient to hold the decedent to an ascertainable standard in distributing trust corpus. **Forsee v. United States, 76 F. Supp.2d 1135 (D. Kan. 1999).**

TRUSTS. The taxpayers, husband and wife owned a photography business for which the husband was the sole employee. The taxpayers established an asset management trust and transferred all their assets to the trust. The trust also established several sub-trusts, including a charitable trust, a vehicle trust and a business trust. None of the trusts operated any business or investments and the taxpayers, as trustees, maintained the same control over the assets as before the transfers. The taxpayers funneled all their income through the trusts and deducted their personal expenses from the trust income. The court held that the trusts were shams and that income from the taxpayers' business was taxable to the taxpayers. The court also disallowed the deductions claimed for the expenses for establishing the trusts, for purchasing the trust kits and for management fees paid to the trust promoters. **Muhich v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,199 (7th Cir. 2001)**.

VALUATION OF STOCK. The taxpayers owned a holding company which owned the stock of a bank corporation. The taxpayers transferred blocks of stock to their children representing a 13 percent interest in the holding company. The court adopted the taxpayers' expert's valuation of the fair market value of the stock, using the net asset value basis method. The taxpayers' expert applied the Quantitative Marketability Discount Model proposed by Z. Christopher Mercer in *Quantifying Marketability Discounts* for determining the minority interest and lack of marketability discount but the court rejected that method as unreliable. The court held that the fair market value of the stock would be discounted 40 percent for the minority interest and 40 percent for lack of marketability. **Janda v. Comm'r, T.C. Memo. 2001-24**.

The decedent was the major shareholder in a family corporation and was 92 years old when the family decided to change the decedent's interest so as to protect the family ownership of the corporation. The decedent agreed to transfer all the stock to a trust for the decedent with remainders to family members. The stock was valued at $100 for gift tax purposes and gift tax returns were filed for the gifts of the remainder interests. The donees also agreed to pay any additional gift tax if the value of the gifts were increased by the IRS and to pay any additional estate tax if the gifts were included in the decedent's estate. The IRS did increase the value of the gifts and the gifts were included in the decedent's estate because the decedent died within three years after the gifts were made. The additional gift tax and estate, however, was paid by other family members and not the donees. The estate contested the valuation of the stock transfers, arguing that the potential gift and estate tax liability of the donees reduced the value of the stock. The court held that the liability for the gift and estate taxes was too contingent to affect the value of the stock at the time the gifts were made. The court also noted that the gift and estate tax liability was illusory because the donees did not pay the additional taxes. **Armstrong v. United States, 2001-1 U.S. Tax Cas. (CCH) ¶ 60,392 (W.D. Va. 2001)**.

FEDERAL INCOME TAXATION

BUSINESS EXPENSES. The taxpayer was the sole shareholder of a trucking business. The taxpayer claimed a business expense deduction for Christmas time gifts of gift certificates to business clients, gift nut baskets to employees and to business clients and $100 bonuses to employees. The court held that the deduction for the gift certificates was limited, under I.R.C. § 274(d), to $25.00 each because the certificates were given to specific individuals and not to the general business entity for use as it determines. However, the court held that the gifts of nut baskets to employees were not limited to $25.00 because the baskets were not gifts, under I.R.C. § 274(d), since the baskets were not excludible from the employees' income under I.R.C. § 102(c)(1). The court also held that the $100 bonuses were deductible as compensation. **Leschke v. Comm'r, T.C. Memo. 2001-18**.

DISCHARGE OF INDEBTEDNESS. The taxpayers operated a dairy farm and owed the FmHA (now FSA) on two mortgages but were unable to make the payments. The taxpayers applied for loan restructuring but were denied. However, the FmHA offered to allow the taxpayers to purchase the loan for the net recovery value (current value of the assets less costs of foreclosure) if they agreed to sign a recapture agreement for the remaining balance of the loans. Under the recapture agreement, the FmHA retained a mortgage on the farm property for 10 years, under which the FmHA retained the right to repayment of the lesser of the fair market value of the property or the remainder on the original loan if the taxpayers sold the property during the next 10 years. The remainder amount was fixed at the time of the agreement and did not increase with interest. The taxpayers argued that no discharge of indebtedness occurred upon the purchase of the mortgage at the net recovery value because the taxpayers remained obligated on the remainder amount. The court characterized the repurchase agreement as a replacement obligation and held that the recapture agreement was too contingent to function as a replacement for the original debt, in that the taxpayers had control over whether the obligation would ever arise, no interest was charged and no date was set on which the obligation would be due. Therefore, the court held that, upon the purchase of the original loan at the net recovery value, the taxpayers had discharge of indebtedness income equal to the difference between the total loan balance less the amount paid to purchase the loan. Note: This was not a case involving a shared appreciation agreement which requires payment of a portion of all appreciation during the term of the agreement whether or not the property is sold. The *Digest* will publish an article by Neil Harl on this case in a later issue. **Jelle v. Comm'r, 116 T.C. No. 6 (2001)**.

DISASTER PAYMENTS. On January 18, 2001, the president determined that certain areas in Vermont were eligible for assistance under the Disaster Relief and Emergency Assistance Act, 42 U.S.C. § 5121, as a result of severe storms and flooding on December 16, 2000. **FEMA-1358-DR**. On January 17, 2001, the President determined that certain areas in Illinois were eligible for assistance under the Act as a result of snow storms beginning on December 10, 2000. **FEMA-3161-EM**. On January 24, 2001, the President determined that certain areas in Indiana were eligible for assistance under the Act as a result of record snow beginning on December 11, 2000. **FEMA-3162-EM**. On January 24, 2001, the President determined that certain areas in Wisconsin were eligible for assistance under the Act as a result of record snow beginning on December 11, 2000. **FEMA-3163-EM**. Accordingly, a taxpayer who sustained a loss attributable to the disasters may deduct the loss on his or her 1999 federal income tax return.

IRA. The taxpayer received distributions from an IRA included in the taxpayer's father's estate. The father's will provided that the heirs would not be liable for any income or estate taxes from distributions from the estate. The taxpayer argued that the distributions were not included in gross income because the distributions represented nondeductible contributions made by the father. The court held that the distributions were included in gross income because the taxpayer did not present any evidence to prove that the father made any nondeductible contributions to the IRA. In addition, the court held that the will provisions did not control the liability for the taxes, at least as between the IRS and the taxpayer. This case is a Tax Court summary decision which cannot be cited as precedent. **Spuler v. Comm'r, T.C. Sum. Op. 2001-8**.

INSTALLMENT METHOD OF REPORTING. The taxpayer sold stock in another corporation. The purchaser paid in cash and a promissory note. The sales agreement required the purchaser to obtain a line of credit sufficient to pay the balance of the note but allowed the taxpayer to draw on the line of credit only if the purchaser defaulted on any installment payment. The IRS ruled that the line of credit did not represent a constructive receipt of the full purchase price in the year of sale because the taxpayer was not fully entitled to withdraw from the line of credit. **Ltr. Rul. 200105061, Sept. 22, 2000**.

RETURNS. The IRS has announced that the required use of revised Form W-9, Request for Taxpayer Identification Number and Certification (Rev. December, 2000), is optional until July 1, 2001. The major change appearing on the revised form is that a payee must certify that he or she is a U.S. person (including a U.S. resident alien). A foreign person may not use Form W-9 to furnish his or her taxpayer identification number to a payor after December 31, 2000. Rather, foreign payees must use the appropriate Form W-8. **Ann. 2001-15, I.R.B. 2001-__**.

The IRS has announced the release of Publication 547, revised December 2000. The publication explains the tax treatment of casualties, thefts and losses on deposits. This document is available at no charge (1) by calling the IRS's toll-free telephone number, 1-800-829-3676; (2) via the internet at http://www.irs.gov/prod/cover.html; (3) through FedWorld; or (4) by directly accessing the Internal Revenue Information Services bulletin board at (703) 321-8020.

SALE OF RESIDENCE. The taxpayer's former spouse had owned a house which was purchased prior to their marriage. During the marriage, the spouse retained title to the property, although the taxpayer paid the mortgage, insurance, taxes and maintenance expenses. The couple divorced and the divorce decree awarded the possession of the house to the spouse but required the house to be sold within eight years and the taxpayer to receive one-half of the net proceeds. The divorce decree stated that title was to remain in both parties' names, although no transfer of title was ordered or accomplished. The taxpayer was also ordered to continue to make the payments for the mortgage, insurance and taxes on the house until it was sold. The IRS argued that the proceeds paid to the taxpayer were capital gains from the sale of a residence because the taxpayer had an ownership interest in the house, evidenced by the terms of the divorce decree. The court held that the taxpayer did not own an interest in the residence because no portion of the title was transferred to the taxpayer by the divorce decree. **Suhr v. Comm'r, T.C. Memo. 2001-28**.

This letter ruling involves I.R.C. § 121 before amendment in 1997. The taxpayer owned a house which was transferred to a trust. The trust provided that the taxpayer could use the house as a residence or sell the house for replacement property. The trust also allowed the taxpayer to withdraw each year up to $5,000 or 5 percent of the aggregate market value of trust corpus. The withdrawal right was non-cumulative. The IRS ruled that the taxpayer was considered to be the owner of so much of the trust as the taxpayer has refused to withdraw each year. The ownership interest was not increased by the right to occupy or sell the house because the taxpayer could not transfer the house or proceeds to the taxpayer. Therefore, if the trust sold the house, that portion of the gain allocated to the taxpayer's accumulated interest in the trust would be eligible for the Section 121 exclusion if the taxpayer was age 55 or older. **Ltr. Rul. 200104005, Sept. 11, 2000**.

SIMPLIFIED EMPLOYEE PLAN. The taxpayer was a shareholder in an S corporation which provided consulting services. The other shares were owned by family members. They filed only one income tax return, in 1987. During the tax years involved in this case, the corporation did not file any returns and the taxpayer performed consulting services free for charitable organizations. The corporation maintained a SEP for the taxpayer and the taxpayer claimed deductions for contributions to the SEP in the tax years involved here. The taxpayer also claimed self-employed health insurance deductions. The court held that the taxpayer was not entitled to either deduction because the taxpayer was not self-employed during the tax years involved because the corporation did not have any income. This case is a Tax Court summary decision which cannot be cited as precedent. **Spuler v. Comm'r, T.C. Sum. Op. 2001-8**.

TAX SHELTERS. These cases involved taxpayers who invested in a partnership which developed and operated jojoba farms. The taxpayer claimed tax losses more than double the initial investment in the first tax year and additional losses in following years. The losses were disallowed because the partnership was held to be a sham tax shelter. The issues in this case were whether the taxpayer was liable for the negligence component of the accuracy-related penalty and whether the IRS should have waived the understatement of tax component of the accuracy-related penalty. The court ruled that the taxpayer had sufficient business acumen that it was unreasonable for the taxpayer to not have sought expert tax advice before claiming substantial and accelerated tax losses more than double the initial investment. The taxpayer also failed to provide any substantial authority for their claim of losses. **Robnett v. Comm'r, T.C. Memo. 2001-17.**

NEGLIGENCE

RECREATIONAL IMMUNITY. The plaintiff was injured while hunting in a tree stand which collapsed. The tree stand was constructed by the nephew of the property owners. The nephew used the tree stand for hunting and allowed the plaintiff to use the tree stand for hunting. The plaintiff sued the nephew, who was represented by the nephew's insurance company. The defendant claimed that the nephew was immune from liability under Wis. Stat. § 895.52 because the injury occurred on the defendant's property while used for recreational purposes. The major issue was whether the statute could apply to a tree stand located on real property owned by third parties. The court held that "property" under the statute included structures, whether or not the owner of the structure also owned the underlying real property; therefore, the accident was covered by the recreational immunity statute and the defendant was not liable for the plaintiff's injuries. The court noted that the holding was consistent with the purpose of the statute in promoting recreational use of rural property. **Peterson v. Midwest Security Ins. Co., 617 N.W.2d 876 (Wis. Ct. App. 2000)**.

ECONOMIC DAMAGES. The plaintiffs entered into a contract with the defendant to custom feed cattle owned by the plaintiffs. The contract required the defendant to care for the cattle "in accordance with the customary standards of care, responsibility, and good animal husbandry." The plaintiffs were unhappy with the investment returns and sued the defendant under contract and negligence theories for improper management of the cattle in violation of the duty of care clause. The contract claims were dismissed but the plaintiffs were awarded damages under the negligence claim by a jury. The defendant argued that no claim in tort could arise from the contract because the plaintiffs alleged only economic losses. The court held that the plaintiffs failed to show any duty owed by the defendant other than the duty of care clause, which arose under the contract; therefore, no tort claim was allowed to enforce the contract. The court also rejected the plaintiffs' claim that a common law duty existed to design and implement the cattle feeding program to protect the plaintiffs' investment. **Grynberg v. Agri Tech Inc., 10 P.3d 1267 (Colo. 2000), *aff'g*, 985 P.2d 59 (Colo. Ct. App. 1999)**.

CITATION UPDATES

Dykes v. Scotts Bluff Cty. Ag. Society, 617 N.W.2d 817 (Neb. 2000) (recreational immunity) see 11 *Agric. L. Dig.* 151 (2000).

McNamara v. Comm'r, 2001-1 U.S. Tax Cas. (CCH) ¶ 50,188 (8th Cir. 2000) (rent as self-employment income) see Harl article p. 9 *supra*.

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by Neil E. Harl and Roger A. McEowen

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